

**Brian Williamson**

**Platforms – making markets work**

**How platform market governance evolves to sustain a healthy market**

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### *Disclaimer*

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# 1. Executive summary

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Platforms - multi-sided marketplaces - are as old as the bazaar, but online platforms have opened up new possibilities for exchange from on-demand transportation to home sharing.

A common feature of online platforms is that they must govern their community or marketplace in order to promote trust and benefit all users including business users, consumers and peer-to-peer participants - if they are to succeed. Platforms compete to offer governance aligned with users' needs, as Jean Tirole put it in 'Economics for the Common Good' in 2017:

*"A two-sided platform interacts both with the seller and the customer. This means that it cares about the customer's interests. This is not philanthropy. A satisfied customer will pay more to the platform, will be more inclined to return. This underlies the uniqueness of the two-sided platform business model." Page 391*

Online platforms are, of necessity, rule-makers who provide governance for market participants, arguably increasing and diversifying regulation relative to conventional externally imposed regulation of markets. A natural question is how well platform owners' interests are aligned with those of participants. The growth and variety of online platforms implies that incentives must be reasonably well aligned, or platforms would not have flourished in competition with conventional business models.

OECD consumer survey evidence from 2017 also shows that consumers trust online platforms more than conventional businesses, and that trust in the platform itself was more important than trust in individual platform participants.

There is also a growing body of evidence looking at outcomes and quality in relation to online

platform markets which tends to confirm that outcomes are good, compared to conventional markets.

Platforms may also use data to reduce social externality, as Airbnb sought to do when they introduced reporting mechanism for neighbours of hosts in relation to nuisance.

When contemplating the application of existing consumer protection and other regulation to platforms, consideration should therefore be given to the regulatory function that platforms themselves are undertaking, and the potential interaction between the two forms of governance.

Platforms can use real-time data to inform governance and constantly adapt as circumstances change. They must maintain a balance between the interests of different platform participants, and at times exclude users to protect consumers and the reputation of the marketplace. Ill-judged regulation could impede this process, harming legitimate market participants and consumers.

For example, ill-conceived regulation related to 'fairness' for business users could undermine the balancing act and ongoing evolution critical to the success of platforms. Doing so could result in consumer harm, in turn harming the interests of businesses participating in platform marketplaces and resulting in further consumer harm.

Governments have a legitimate interest in outcomes in relation to online platform markets, but the best means of achieving good outcomes should be assessed mindful of the market governance role platforms play, the reasons they have proved successful and the limitations and potential unintended consequences of regulation.

## 2. The nature of multi-sided (platform) markets

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Platforms are multi-sided marketplaces which bring different parties together to transact. Core to the definition of platforms is their multi-sided nature;<sup>1</sup> apps stores, eBay and Airbnb are online platforms; whilst Amazon Cloud Services (AWS) and Netflix are not because they provide services themselves rather than an arms-length marketplace for others.

A medieval market was a platform with rules such as how produce was measured and the location and time at which trade could occur. It brought a limited number of traders, with a limited range of goods and services, together to create a more efficient market. A key challenge was creating a functioning market in conditions of scarcity.

Online platforms use computation and communications technology to facilitate transactions and can accommodate large numbers of participants and may be global (transactions may be global or local).

As Jean Tirole put it, the challenge of market organisation is shifting from managing scarcity to managing abundance.<sup>2</sup> Whereas previously markets including offline platforms sought to bring parties together and promote efficient trade in conditions of scarcity:

*“While, for millennia, our ancestors had trouble finding trading partners, now our problem is identifying, among the millions of partners with whom we could trade, the one that best corresponds to our expectations. We suffer from too much choice, not too little....” Page 380.*

Now the challenge is ensuring an efficient match when the number and diversity of participants is abundant:

*Thus, the most significant transaction costs are no longer transportation costs, but rather assessing what is on offer and choosing who to do business with, along with the signaling costs (seeking to convince potential trading partners of one’s reliability). Our almost infinite sources of information, and the limited time we have to process and understand them, put the intermediators and platforms that help us find these partners at the heart of the economic process.” Page 381*

Platforms therefore process information, including information regarding reputations and preferences, to facilitate matching and trade. To be effective they must endeavour to best meet the needs of both sides of the market, which involves market governance (via terms of service) and the disciplining or exclusion of participants who do not play by the rules.

Platforms are ‘regulators’ by necessity but must compete and adapt in terms of how they regulate the market to ensure it works in the interests of users overall. As Arun Sundararajan put it:<sup>3</sup>

*“Despite some regulators’ fears, the sharing economy may not result in the decline of regulation but rather in its opposite: both an increase and a diversification of regulation.” Page 138*

Both the market and market governance are constantly evolving driven by users’ preferences, technological change and unanticipated developments (for example, identification of an exploit by a bad actor).

The evolution of platforms is fundamentally a bottom-up process driven by users’ needs,

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<sup>1</sup> Hagiu and Wright, [Multi-Sided Platforms](#), Harvard Business School Working Paper 15-037, March 2015.

<sup>2</sup> Jean Tirole, *Economics for the Common Good*, 2017.

<sup>3</sup> Arun Sundararajan, *The sharing economy*, 2017.

technological change and the need to mitigate harm due to bad actors. As John McMillan put:<sup>4</sup>

*“The platform for a market in large part evolves by trial and error. The mechanisms for transacting develop from the bottom up, via innovations made by the participants. Spontaneous evolution is the main driver of markets.” Preface*

In terms of technology, changes include the development of wireless data networks, smartphones and apps over the past decade, enabling new types of online platforms including peer-to-peer transportation services. Developments in machine learning enable new interfaces (including voice and image recognition), information processing and matching mechanisms and opportunities for more refined market governance. We are at an early stage in terms of the evolution of online

platforms, with technology and the market constantly changing.

Online platform-based markets will continue to expand into new areas, and to evolve. Market governance - expressed via terms of service and their day-to-day application - will, and needs to, adapt faster than would be possible under top-down law and regulation.

In order to understand the changing role of regulation in relation to platform-based markets, which provide and adapt their own governance, it is crucial to consider whether their incentives are aligned with the interests of users of the marketplace; and what impact different forms of external regulation might have on the system as a whole. The remainder of this paper addresses these questions.

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<sup>4</sup> John McMillan, *Reinventing the Bazaar – a natural history of markets*, 2002, Norton.

### 3. Platforms have an incentive to act in users' interests

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In order to create and sustain an online marketplace, platforms have an incentive to design a set of rules - expressed via their terms of service and decisions enforcing those terms of service - which promote the interests of market participants overall. As Jean Tirole (2017) put it:

*"A two-sided platform interacts both with the seller and the customer. This means that it cares about the customer's interests. This is not philanthropy. A satisfied customer will pay more to the platform, will be more inclined to return. This underlies the uniqueness of the two-sided platform business model." Page 391*

Another commentator remarked on the dependence of platforms on continued participation of buyers and sellers in multi-sided markets:<sup>5</sup>

*"Amazon, Facebook, Google, Baidu, Tencent, Alibaba, Uber, Twitter and co have nothing but a critical mass of buyers and sellers, content producers and content consumers, drivers and passengers that are connected through their platforms. Their platforms then need to manage the behaviours of their constituencies: in other words, to be good governors."*

Platforms must help match parties to a transaction, and help participants decide who to trust. When the terms of service are broken, or new threats to trust and the health of the marketplace emerge, participants may be disciplined or excluded; and the exercise of a degree of discretion in decision making and freedom to change the terms of service are necessary given the incompleteness of any set of

rules and the need to adapt them as circumstances change.

The health of the marketplace may trump the interests of an individual user (who may not be benign). However, the commercial interests of the platform owner are aligned with the success of the market overall and therefore with legitimate users' interests. This alignment of interests may also involve investment in an ecosystem that extends beyond the marketplace itself.

For example, providers of apps stores invest in the underlying infrastructure including operating systems and application programming interfaces (APIs) for developers, developer tools such as the open sourced Apple Swift programming language, training<sup>6</sup> and via marketing support for developers. Curation of apps in stores helps ensure discovery and valued matches, whilst secure and simple payments mechanisms facilitate trade. Investment in the entire ecosystem is required for success.

Participation in apps stores is subject to published terms of service, and apps may require pre-approval, and/or ongoing monitoring, to promote a quality marketplace and protect consumers from harm.

At times swift action, potentially without notice, is required to remove apps which violate legal requirements such as Copyright, or harm users, for example, via malicious code or inappropriate content. Leaving a harmful app in the store would not only harm users but would harm legitimate developers to the extent that trust in the marketplace was diminished. Not only is swift action required at times, a judgement call

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<sup>5</sup> Chris Skinner's Blog, Will platforms replace governments?, 2018. <https://thefinanser.com/2018/02/will-platforms-replace-governments.html/>

<sup>6</sup> For example, at developer conferences and the iOS Developer Academy in Naples.

<https://www.apple.com/newsroom/2016/10/apple-opens-first-ios-developer-academy-in-naples/>

regarding grey areas or the balance of risk may also be required.

Continued entry, growth and diversification in relation to online platform-based markets suggests that incentives are well aligned. If they were not, service providers and customers would not find online platforms attractive relative to other market mechanisms or competing platforms that more effectively governed their respective marketplaces.

Further, whilst society has wider interests than those of individual platform users or owners (including: consumer, environmental and data protection and ensuring markets remain contestable), horizontal law applies to platforms as well as other market institutions.

Platforms are also able to use their ability to process information coupled with their terms of service to discipline behavior, including behavior which harms non-platform participants. For example, in 2016 Airbnb introduced a system that allows neighbors to share specific concerns they might have about a listing in their community.<sup>7</sup>

The appropriate role of legislation and regulation alongside the governance provided by platforms is considered in the final section of this paper. However, we first consider evidence in relation to the alignment of interests including how governance has evolved, the growth of platforms, consumer survey evidence and empirical studies relating to platform market outcomes.

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<sup>7</sup> <https://blog.airbnb.com/new-resource-for-neighbors/>



## 4. Experience suggests alignment with users' interests

Online platforms govern their marketplaces via terms of service, monitoring and judgement. The evolution of governance over time sheds light on the question of alignment of interests, and on the possible consequences of regulation.

### Apps stores

Apple, Google and others including Tencent (MyApp) provide app store platforms. We focus on the Apple app store, which opened to developers in July 2008. App developers operate within a software development environment which helps ensure security and protect user's,

and the apps store is curated to promote it as a valued marketplace for developers and users.

These elements continuously evolve - to support new possibilities in relation to apps development, new opportunities for monetisation and to address issues that arise in relation to conduct over time. Apps may be removed from the store to improve marketplace quality, at times without notice where an app presents a threat of harm to consumers or to trust in the marketplace. Illustrative examples of changes are shown in Figure 1.

Figure 1: Illustrative changes introduced by Apple for its apps store

Change	Comment
In 2010 detailed guidance for developer was published. <sup>8</sup> The guidelines have developed over time. <sup>9</sup>	The guidelines were a response to the need for greater clarity over app approval and removal. However, the guidelines necessarily require interpretation and judgement, and at times apps are removed without notice where they are found to constitute a threat to consumers or the reputation of market.
In 2016 the app store commission was reduced from 30% to 15% for all recurring subscriptions.	This was designed to better reward developers and encourage more 'professional' apps onto the platform. <sup>10</sup>
Apps that were clones of other apps were removed from the store in 2017. <sup>11</sup>	This measure improved the quality of the store, thereby benefiting consumers and most developers, though clearly not in the interests of the developers of app clones.
A number of apps that shared user's location were removed in 2018. New app store terms have also been introduced requiring all new apps and updates to have a privacy policy from 3 October 2018. <sup>12</sup>	Use of personal information such as location can enhance consumer benefits but may also result in harm. The underlying technology (for example secure storage of facial recognition data on the device) and terms of service evolve protect consumers privacy whilst also allowing users to benefit from enhanced and personalised services.

<sup>8</sup> Wired, [Apple answers questions about app rejections, raises others](#), September 2010.

<sup>9</sup> <https://developer.apple.com/app-store/review/guidelines/#location>

<sup>10</sup> John Gruber commented "I think it's truly win-win-win, for Apple, its users, and most importantly for developers."

The New App Store: Subscription Pricing, Faster Approvals, and Search Ads, 8 June 2016.

[https://daringfireball.net/2016/06/the\\_new\\_app\\_store](https://daringfireball.net/2016/06/the_new_app_store)

<sup>11</sup> TechCrunch, [Apple goes after clones and spam on the apps store](#), June 2017.

<sup>12</sup> <https://itunespartner.apple.com/en/apps/news/100002362>

## Transportation

Online platforms are transforming transportation with peer-to-peer car rental e.g. Hiyacar, long-distance car sharing e.g. BlaBlaCar and taxi services e.g. Taxify, Cabify and Uber. Hiyacar (started in the UK) is a peer-to-peer car rental platform.<sup>13</sup> With the installation of a 'QuickStart' box, cars can be unlocked with a smartphone app. Car owner's set car hire times and prices and receive 70% of the rental. Insurance supersedes the car owner's policy for the duration of the hire.

BlaBlaCar (started in France) offers ride sharing for longer journeys, with passengers contributing to costs. BlaBlaCar provide a range of safety features including profiles, ratings and secure communications.<sup>14</sup>

Taxify (started in Estonia) and Cabify (started in Spain) offer peer-to-peer transportation platforms. They incorporate features to protect users and promote a safe and efficient marketplace, for example the Taxify driver app includes an SOS button for use in case of medical emergencies or accidents.<sup>15</sup>

A general feature of smartphone platform-based transportation services is recording of the identify of users and GPS based tracking. This provides a data driven form of market governance, largely absent from conventional taxi services where regulation has focussed primarily on entry criteria.<sup>16</sup>

In Figure 2 we consider changes introduced by Uber over time to improve passenger and driver protection and to better reward drivers.

Figure 2: Illustrative changes introduced by Uber peer-to-peer transportation

Change	Comment
Driver or passenger accounts may be deactivated permanently or temporarily if the terms of service (community guidelines) are not followed. <sup>17</sup>	Deactivation may be immediate or follow feedback regarding conduct or ratings which does not result in the required change in behaviour, depending on the circumstances. This necessary feature to protect users would be unworkable if there were a minimum notice period (as proposed in a European Commission regulation for platform to business relationships).
In 2015 phone number anonymisation for users was introduced.	This change followed instances of misuse of personal contact information by some drivers. <sup>18</sup>
In 2016 a pilot program was introduced to verify feedback using smartphone technology (Gyrometers, GPS and accelerometers) to show how often a vehicle starts and stops, as well as its overall speed.	This change was motivated by the fact that user ratings may not always be fair or accurate. Data from the driver's app can be used to monitor some aspects of behaviour as a means of verifying user feedback.
In 2018 Uber tested 'Ride Check' to check for unusual decelerations. <sup>19</sup>	Deceleration, coupled with other information, can indicate an accident or an unusually long stop. Machine learning is used to interpret the data.
Uber have introduced driver insurance, driver hours limits <sup>20</sup> and a tips feature within the app to improve the quality and remuneration.	These changes were motivated by competition for drivers, driver feedback and a desire to offer a quality service to users.
In 2018 Uber announced that drivers who maintain high ratings and low cancellation rates can earn rewards including increased earnings and free college tuition. <sup>21</sup>	The initiative is motivated by competition for drivers and as an incentive for improved service.

<sup>13</sup> <https://www.hiyacar.co.uk>

<sup>14</sup> <https://www.blablacar.co.uk/trust-safety-insurance>

<sup>15</sup> <https://support.taxify.eu/hc/en-us/articles/360004091574-Using-the-SOS-Button>

<sup>17</sup> <https://www.uber.com/en-GB/legal/community-guidelines/uk-en/>

<sup>18</sup> Uber, *Introducing phone anonymisation*, 2015.

<sup>19</sup> The Verge, *Uber is going to turn your smartphone into an automatic crash detector*, September 2018.

<sup>20</sup> <https://www.uber.com/en-GB/blog/driver-hour-limits/>

## Home sharing

Home sharing platforms include house-swapping (e.g. Lovehomeswap), short-term rentals (e.g. Onefinestay and Airbnb) and sharing communities (e.g. Couchsurfing).

The founder of Lovehomeswap started an industry association for sharing economy businesses in the UK which has developed a quality assurance mark - 'TrustSeal' - developed in conjunction with the Oxford University SAID business school.<sup>22</sup> This

initiative illustrates that not only do platforms seek to promote trust in their marketplaces but may also establish systems for external validation. Initiatives such as this may be particularly valuable for smaller platforms able to rely less on brand, at least initially.

In Figure 3 we focus on illustrative examples of the development of platform governance by Airbnb (an overview of the approach of Airbnb to building trust is provided in an article in Medium<sup>23</sup>).

Figure 3: Illustrative changes introduced by Airbnb peer-to-peer home sharing

Change	Comment
In 2014 the review system was changed so that reviews were revealed simultaneously to host and guest. <sup>24</sup>	The motivation for this change was to remove the concern of both hosts and guests that if they leave an honest review that includes praise and criticism, they might receive an unfairly critical review in response.
In 2016 a system for reporting antisocial behaviour by guests was introduced for neighbours. <sup>25</sup>	This change responded to concern regarding those guests who imposed costs on neighbours, such as noise. It illustrates how a platform may act to address externalities.
In 2017 the review system was changed so that reviews could be left by a guest who left early.	This change addressed a concern that poor-quality experiences would not result in a review if the guest left early as a result. This change was made following concern expressed by the UK Competition and Markets Authority. <sup>26</sup> This example illustrates the balancing act required between host and guest rights, but also that general consumer protection law has been applied in practice to platforms.

<sup>20</sup> <https://www.uber.com/en-GB/blog/driver-hour-limits/>

<sup>21</sup> The Verge, Uber will start rewarding high-performing drivers with better earnings and free college tuition, November 2018. <https://www.theverge.com/2018/11/1/18047746/uber-driver-high-performing-earnings-free-college-tuition-pro>

<sup>22</sup> <https://sharingeconomytrustseal.com/about/>

<sup>23</sup> Newman and Antin, Building for Trust - Insights from our efforts to distill the fuel for the sharing economy, March 2016. <https://medium.com/airbnb-engineering/building-for-trust-503e9872bbbb>

<sup>24</sup> <https://blog.airbnb.com/building-trust-new-review-system/>

<sup>25</sup> <https://blog.airbnb.com/new-resource-for-neighbors/>

<sup>26</sup> CMA, CMA welcomes Airbnb guest review changes, July 2017. <https://www.gov.uk/government/news/cma-welcomes-airbnb-guest-review-changes>

## 5. Evidence indicates platform market governance is working well

Evidence regarding outcomes in relation online platform markets includes their growth and success, or failure; survey-based evidence; and empirical studies of the quality of outcomes in platform markets.

The three sources of evidence in combination suggest that not only do platforms have an incentive to align their market governance with users' interests, but that outcomes may be superior to those in conventional markets coupled with conventional regulation.

We note that the platform market governance model is still in a fast learning phase in terms of development, and that technologies including the internet of things and machine learning are likely to increase the scope to fine tune market governance in future.

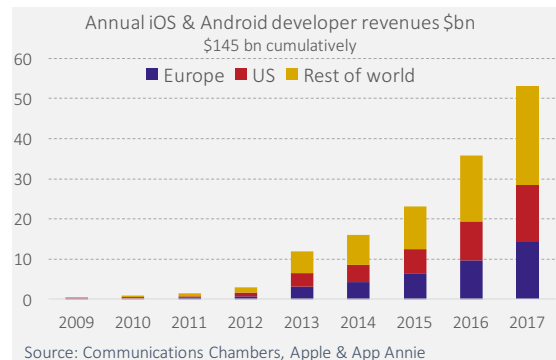
### Growth and success, or failure

We would not be discussing online platforms at all had they not been successful in competition with other forms of market organisation and governance. Not all have succeeded (e.g. the consumer side of the Google+ social network is shutting down following discovery of a bug<sup>27</sup>), but some have thrived, and new online platforms focussed on specific economic verticals are entering the market on an ongoing basis.

An illustrative example of success, in competition with alternative approaches, is the growth of apps store marketplaces. The market continues to grow and diversify, with over 2 million apps in the iOS and Google Play stores respectively and cumulative revenues paid to developers of \$145 bn to 2017. Payments to

European developers approximate those to US developers, as shown in Figure 4.<sup>28</sup>

Figure 4: Developer revenues from app stores



In fact, developer revenues from app stores underestimate overall developer benefits, since direct subscriptions made outside of apps stores (for example Netflix, Spotify and The Economist which offer both outside and within store subscription options) and digital advertising revenues are not reflected in app store payments.

A number of apps are also platforms in their own right, for example, Uber and Airbnb. Any platform fees or commissions charged by these platforms are also not included within app store revenues.

Apps stores have thrived and continue to compete with alternatives including cloud-based web services, online software downloads and physical distribution of software.

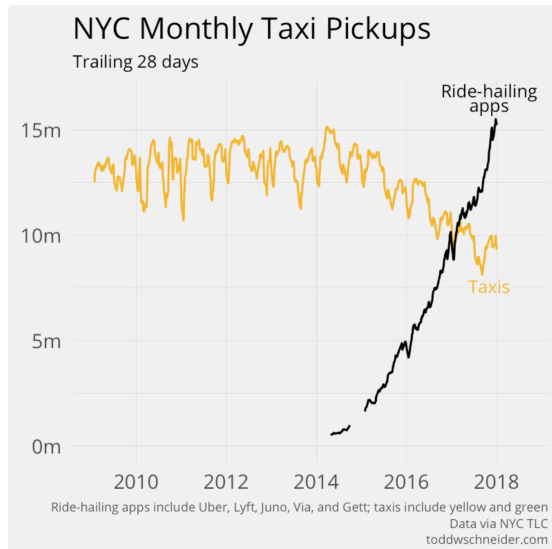
Another example is peer to peer transport services which have grown not only their share but the overall market, by better meeting consumer's needs. Figure 5 shows growth in overall ridership in New York City (if you sum up

<sup>27</sup> <https://www.blog.google/technology/safety-security/project-strobe/>

<sup>28</sup> Estimates based on Apple press releases and App Annie reports of the Android-iOS developer revenue ratio. Regional shares based on Apple Job Creation reports for the US and Europe which provide snapshots of regional revenue shares.

the lines) with Uber and Lyft in particular contributing to overall market growth.<sup>29</sup>

Figure 5: Growth in market driven by peer to peer transport apps



### Survey based evidence

The most informative surveys are comparative, since there will always a level of dissatisfaction

with any matching, trade and allocation mechanism – whether platform, non-platform market based, or non-market based (for example, organ-donor matching).

The OECD carried out a comparative survey of consumer experience in relation to online peer-to-peer platforms, including comparative questions regarding other online and offline businesses.<sup>30</sup> The survey found that whilst around a third of consumers have experienced a problem with an item or service mediated by a platform at some point:

*“Only a small minority of users (on average 10% of users across the ten OECD countries surveyed) trust their peer platform less than conventional businesses in the same market.”* Page 26

Figure 6 shows that overall trust was higher for peer platforms versus conventional businesses in all sectors considered, with the greatest difference for transport services.

Figure 6: Trust in peer platforms versus conventional businesses by market (%)

	Buying	Sharing	Accommodation	Transport	Tasks
More	27	36	26	50	34
About the same	57	54	60	45	53
Less	12	8	11	4	11
<b>Net (more – less)</b>	<b>+15</b>	<b>+28</b>	<b>+15</b>	<b>+46</b>	<b>+23</b>

This result is interesting, given that regulation of legacy taxi services is (ostensibly) for the benefit of users; yet may be performing less well than platform enabled market governance provided by peer-to-peer transport platforms (admittedly alongside some regulation applicable to conventional taxi services, though in some markets this represents a small part of overall market governance).

The OECD survey also found that consumer trust is anchored in the platform and that trust in the seller/provider offering the item or service is important, but not essential for a consumer to go ahead with a transaction. Platforms offer an umbrella in terms of trust in their brand for participants, an umbrella they have an incentive to preserve and build.

<sup>29</sup> Todd Schneider, *Analyzing 1.1 Billion NYC Taxi and Uber Trips, with a Vengeance*, March 2018.

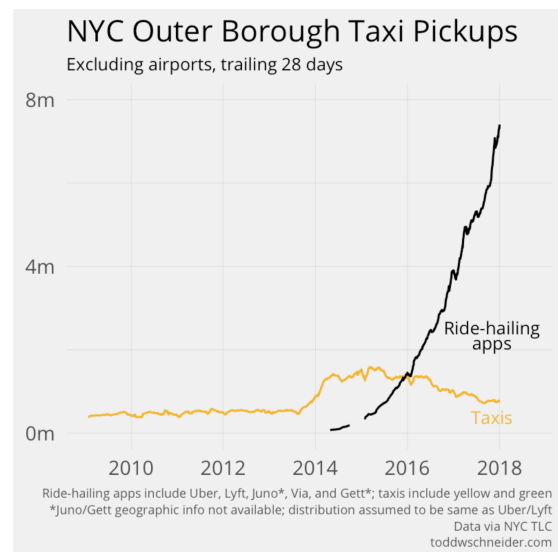
<sup>30</sup> OECD, Trust in peer platform markets, November 2017. [https://www.oecd-ilibrary.org/science-and-technology/trust-in-peer-platform-markets\\_1a893b58-en](https://www.oecd-ilibrary.org/science-and-technology/trust-in-peer-platform-markets_1a893b58-en)

## Empirical market evidence

There is an emerging body of empirical evidence regarding outcomes in platform markets and how well they govern the market to promote trust and good outcomes for consumers.

Studies have considered the efficiency of utilisation for peer-to-peer transport services<sup>31</sup>, quality of service relative to conventional taxi services<sup>32</sup> and growth in service availability in previously underserved areas<sup>33</sup> (see Figure 7 below and compare with the previous Figure 5). Overall the findings are positive.

Figure 7: Peer to peer transport apps serving previously underserved areas



Other evidence shows that reputation badges and buyer protection programs utilised by eBay increased sellers' quality and resulted in a higher exit rate for low-quality sellers<sup>34</sup> i.e. consumers and the overall market benefited, but at the cost of low-quality sellers. This emphasises the importance of a degree of exclusion to the proper functioning of marketplaces.

<sup>31</sup> Castillo, Knoepfle and Weyl, [Surge pricing solves the wild goose chase](#), July 2017.

<sup>32</sup> Liu, Brynjolfsson and Dowlatabadi, Do digital platforms reduce moral hazard? The case of Taxis and Uber, July 2018. National Bureau of Economic Research Working Paper 113125.

<sup>33</sup> Todd Schneider, [Analyzing 1.1 Billion NYC Taxi and Uber Trips, with a Vengeance](#), March 2018.

<sup>34</sup> Xiang Hui, Maryam Saeedi, Zeqian Shen, Neel Sundaresan, [Reputation and Regulations: Evidence from eBay](#), Management Science Volume 62(12), February 2016.

## 6. The role of regulation alongside platform market governance

Previous sections have considered how platform market governance has developed and evolved, and the alignment with users' interests.

The conclusion is positive, platform market governance appears broadly aligned with users' interests, and to be resulting in outcomes that are as good or better than those in conventional markets subject to externally imposed regulation.

Platforms may offer, as Sundararajan (2016) put it, both more and more diverse regulation:

*"Despite some regulators' fears, the sharing economy may not result in the decline of regulation but rather in its opposite: both an increase and a diversification of regulation." Page 138*

Platforms will produce diverse forms of regulation or market governance in competition to one another, but not in a race to the bottom but in a race to the most efficient and effective form of regulation consistent with the overall health of the marketplace and consumers interests. Whilst platforms compete over market governance, they nevertheless act to facilitate a single market across borders.<sup>35</sup>

A European Commission Joint Research Centre study also recognised the role of platforms in providing market governance and implication that, should regulation be required, it would differ in character from regulation of non-platform markets:<sup>36</sup>

*"The emergence of news types of online (collaborative) platforms has led to some*

*substitution in activity between traditional firms and new market places. This has triggered calls for the creation of a regulatory playing field between traditional and new online market places. Some have called for a wholesale extension of existing regulatory frameworks, or at least a partial extension that could lead to market fragmentation between smaller and larger producers of online services.*

*It would be preferable to first of all take into account the capacity for online platforms to auto-regulate their specific markets. That may of course lead to new types of market failures in search rankings, review ratings and the management of contingent risks in transactions. This might require meta-regulation of these potential market failures. Again the message is that regulation should not protect incumbent business models but support welfare-enhancing innovation."*

Whilst platforms are motivated to govern multi-sided markets in the interests of users, questions nevertheless remain.

### Externalities

Incentives may be aligned with those of platform users, but externalities may arise for non-users. As Arun Sundararajan noted:<sup>37</sup>

*"The trick is to identify those dimensions of risk where the incentives of the platform and the incentives of society (or of consumer protection) don't diverge, and*

<sup>35</sup> Matthias Bauer, Online Platforms, Economic Integration and Europe's Rent-Seeking Society: Why Online Platforms Deliver on What EU Governments Fail to Achieve, October 2018. <http://ecipe.org/publications/online-platforms-economic-integration-europes-rent-seeking-society/>

<sup>36</sup> Bertin Martins, An Economic Policy Perspective on Online Platforms, 2016. European Commission Joint Research Centre Working Paper 2016/05. <https://ec.europa.eu/jrc/sites/jrcsh/files/JRC101501.pdf>

<sup>37</sup> Arun Sundararajan, The sharing economy, 2017.



*those where the risk of divergence exists. For example, ensuring that hosts advertise their quality accurately seems well aligned with Airbnb's profit motive, while ensuring that guests do not make too much noise when staying in an Airbnb might be less aligned.” Page 148*

Platforms themselves may address some of these for reputational reasons, for example the introduction by Airbnb of a reporting mechanism for neighbours of renters. The trust building mechanisms introduced by platforms may also promote trust and social cohesion more generally, for example by helping to overcome social bias.<sup>38</sup>

Further, to the extent that regulation of externality is justified, it should not in general be specific to platforms, but should target the externality in question. For example, a carbon tax or congestion charge should apply to all sources of CO<sub>2</sub> emissions or congestion respectively.

### **Reconciling platform market governance and regulation**

We are also left with the task of reconciling private market governance – expressed via terms of use and their interpretation for platforms – with existing law and regulation.<sup>39</sup> Applying a ‘level playing field’ of the old rules for the new is seldom, if ever, going to be the right answer. First, because doing so may entrench traditional business models and shelter them from innovation and competition. Second, because platforms themselves provide

governance which differs from, and may in key respects is superior to existing regulation.

As the European Commission put it in relation to the collaborative economy:<sup>40</sup>

*“The collaborative economy is a good example where rules designed with traditional and often local service provision in mind may impede online platform business models.” Page 5*

Brand also plays an important role in relation to platform market governance, with the OECD finding that a platform owners’ brand can be more important than the reputation of the individual participants on the platform.<sup>41</sup> However, for the platforms brand to provide a valuable signal to marketplace participants the platform must be able to sanction or exclude participants who would otherwise undermine the brand and marketplace credibility.

Platforms may also band together under a quality mark, for example the ‘TrustSeal’ developed by Sharing Economy UK in partnership with Oxford University SAID business school.<sup>42</sup> Another external standard is ‘TrustPass’ launched by Alibaba in 2001, whereby sellers went through a third-party identity check and bank account verification process.<sup>43</sup>

However, mechanisms such as this are likely to work best where participation is voluntary, and the mechanism operates in competition with alternative governance models i.e. it is not a closed shop. Collective or external reputational mechanisms may also be more effective for less

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<sup>38</sup> Abrahao, Parigi, Gupta, and Cook, Reputation offsets trust judgments based on social biases among Airbnb users, September 2017. PNAS, vol. 114(37). <http://www.pnas.org/content/pnas/114/37/9848.full.pdf>

<sup>39</sup> Brian Williamson and Mark Bunting, [Reconciling private market governance and law: A policy primer for digital platforms](#), May 2018.

<sup>40</sup> European Commission, [Communication on Online Platforms and the Digital Single Market Opportunities and Challenges for Europe](#), May 2016.

<sup>41</sup> OECD, Trust in peer platform markets, November 2017. [https://www.oecd-ilibrary.org/science-and-technology/trust-in-peer-platform-markets\\_1a893b58-en](https://www.oecd-ilibrary.org/science-and-technology/trust-in-peer-platform-markets_1a893b58-en)

<sup>42</sup> <http://www.sharingeconomyuk.com/trustseal>

<sup>43</sup> Rachel Botsman, Who can you trust?, 2017. Page 23.



established brands, or in circumstances where trust is hard to build or needs to be rebuilt.

### **In whose interests should we regulate?**

The purpose of markets is to serve the interests of consumers and citizens, not businesses *per se*.

Platforms, by providing market governance via their terms of service, have been successful because their marketplaces are efficient and govern conduct and quality - turning 'market failures' conventionally addressed via law and regulation into 'market successes'.

Doing so requires not only codes of conduct, but discretion in applying such codes on a day to day basis in order to address emerging threats to the market and consumers' interests on a timely – sometimes immediate – basis. In turn that can necessarily involve rough justice for service providers who engage in harmful, but not necessarily illegal, activities.

Regulation that would shift the balance by seeking to protect business users of platforms on grounds of fairness, as the European Commission is contemplating<sup>44</sup>, could harm consumers and in turn the interests of those businesses investing in and participating in platform marketplaces – without whom consumers interests would be undermined.

Applying constraints on the business relations of online platform-based business models could have a number of unintended consequences, in particular:

First, to the extent that doing so constrains the development of such models it may reduce competition, since platforms have lowered entry barriers for new businesses and helped facilitate competition in markets where competition was previously weak.

Second, if platforms are constrained from exercising discretion and acting swiftly to remove bad actors from platform markets, then not only may individual consumer harm result directly but trust in the marketplace may be diminished – resulting in more general harm.

Third, imposing specific rules in relation to P2B relations may distort the market relative to other business models which may engage in similar practices, for example, prioritising or removing goods or services to improve the quality of their offer overall.<sup>45</sup>

### **Conclusion**

As a rule, it is unwise to seek to promote fairness in P2B relations, or to promote one business model over another, but to ensure that competition and consumers are both protected.

Given platform market governance via their terms of service, less rather than more externally imposed regulation is likely to be consistent with the goal of consumer protection; whilst competition should be protected using appropriate analysis and tools within existing frameworks.

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<sup>44</sup> Separate from ensuring that markets are open to competition.

<sup>45</sup> Traditional retailers necessarily engage in such practices when they decide what to offer and how to place it. They may also offer substitute or competing own-branded products and services.